B.C.D. 04-64

Employer Status Determination
Decision on Reconsideration
American Railroads Corporation

DEC 0 3 2004

This is the decision of the Railroad Retirement Board on the request of American Railroads Corporation (American Railroads) that the Board reconsider the initial determination in Board Coverage Decision 03-56, rendered June 16, 2003, that American Railroads is an employer covered under the Railroad Retirement and Railroad Unemployment Insurance Acts. For the reasons set forth below, the Board determines on reconsideration that American Railroads is an employer covered by the Railroad Retirement and Railroad Unemployment Insurance Acts, effective June 1, 1991.

The evidence on reconsideration consists of a combination of public documents and published material; and of the letters submitted to the Board by officials of American Railroads and associated railroads, in connection with this decision and with earlier decisions of the Board regarding the coverage of other entities affiliated with American Railroads. Considered in roughly chronological order, this evidence establishes the following:

In a letter dated July 1, 1991, Mr. David Enquist, Vice President – Finance of the Texas North Orient Corporation, reported that Texas North Orient began operating a 161 mile line of track between Maryneal and Chillicothe, Texas, which was owned by Texas and Oklahoma Railroad. Based on this information, the Texas and North Orient was determined to be a rail carrier employer covered by the Acts effective June 1, 1991. See: *Texas and North Orient Corporation*, Coverage Notice No. 91-76. That decision remains in effect to date. However, while records of the Board show that Texas and North Orient reported employees through 2002, the report filed in 2004 showed no employees for 2003.

On March 16, 1992, Richard McClure, Robert J. Geib, and Michael Minton as majority shareholders, incorporated the Gulf, Colorado & San Saba Railway (GC&SS Railway) in the state of Texas to acquire and operate approximately 67 miles of track between the towns of Lometa and Brady in that state. See: Gulf, Colorado & San Saba Railway Corporation—Acquisition and Operation Exemption—Atchison, Topeka and Santa Fe Railway Company, Interstate Commerce Commission Finance Docket No. 32216, 57 Fed. Reg. 61921 (December 29, 1992). On August 16, 1993, the Board determined GC&SS Railway to be a covered rail carrier employer under the Acts. See: B.C.D. 93-52, *Gulf, Colorado & San Saba Railway Corporation*. The Board found coverage

began May 11, 1993, the date on which correspondence from GC& SS Railway stated that operations began. A national railroad industry directory currently identifies Mr. Richard McClure as President and Chief Executive Officer of GC& SS Railway. See: Commonwealth Business Media, The Pocket List of Railroad Officials, 4th Quarter 2004, at C-30.

On July 21, 1994, GC&SS Railway incorporated Sweetwater Central Switching Company (Sweetwater Switching) as a wholly owned subsidiary to provide rail switching service connecting with the Burlington Northern Santa Fe Railway in Sweetwater, Texas. The Board determined Sweetwater Switching to be covered as a rail carrier employer under the Acts effective July 21, 1994. See: B.C.D. 03-47 *Sweetwater Central Switching Company*. Though Sweetwater Switching evidently operates in its own name, its employees evidently are reported to the Board as employees of GC&SS Railway.

Sometime in 2002, American Railroads incorporated Missouri & Valley Park Railroad Company (Mo&VP RR) as a wholly owned subsidiary to lease and operate approximately 2 miles of rail in the vicinity of West Valley Park, Missouri. See: Missouri & Valley Park Railroad Corporation—Lease Exemption—The Burlington Northern and Santa Fe Railway Company, Surface Transportation Board Finance Docket No. 34231, 67 Fed. Reg. 50751 (August 5, 2002). Based on information furnished by Richard McClure as President and Chief Executive Officer, the Board on June 10, 2003, determined Mo&VP RR to be a covered rail carrier employer under the Acts effective July 4, 2002. See: B.C.D. 03-48, *Missouri & Valley Park Railroad Company*. The Pocket List of Railroad Officials reports that Richard McClure currently remains in both positions. Id. at C-38.

The investigation into the status of American Railroads began when Mr. Richard McClure responded in a letter dated May 21, 2001, to an inquiry from the Board's Chief of Audit and Compliance regarding the Southern California Railroad, by describing American Railroads as "A shortline holding company and consulting group with several switching and shortline companies. * * * American Railroads Corporation is the executive branch of the South California Railroad, which is the operations revenue building railroad switching devison (sic)." Mr. McClure further stated that American Railroads "owns 100%" of Sweetwater Central Switching, Texas North Orient Corporation, GC&SS Railway, and Southern California Railroad, and that these companies "all create revenues through American Railroads Corporation". In a subsequent letter dated June 25, 2001, Ms. Christine Olson, Controller for the Southern California Railroad, stated that the following officials held the same positions in both Texas North Orient and GC&SS Railway: Richard McClure, President, Treasurer and CEO; Robert Geib, Secretary and Director; and Michael Minton, Director.

The Board determined on the basis of information furnished by Mr. McClure that Southern California Railroad was not a rail carrier employer covered by the Acts because it served only one shipper. See: B.C.D. 01-75, *Southern California Railroad Company*. However, in view of Mr. McClure's description of American Railroads in connection with the *Southern California Railroad* decision, the Board's Chief of Audit and Compliance by letter dated August 16, 2001, posed to Mr. McClure several questions regarding the business operations of American Railroads in order that its status as a covered employer under the Acts might be resolved. Mr. McClure did not respond to that letter, nor to further inquiries by the Chief of Audit and Compliance on October 4, 2001, November 5, 2001, or January 8, 2002. On May 15, 2002, the Chief of Audit and Compliance then issued an administrative subpoena to Mr. McClure, which required that he furnish the information. When Mr. McClure failed to respond to the administrative subpoena, the Board's Office of General Counsel warned by letter of June 27, 2002, that in the case of contumacy, section 12(b) of the Railroad Unemployment Insurance Act empowered the Board to invoke enforcement in United States District Court. Receiving no reply, the United States Attorney for the Northern District of Illinois on March 26, 2003 filed a petition on the Board's behalf for summary enforcement in the United States District Court. By agreement with the United States Attorney, Mr. McClure then responded to the Chief of Audit and Compliance by letter dated April 2, 2003, further supplemented by a letter dated April 28, 2003 by counsel for American Railroads. The enforcement action was then voluntarily dismissed. See: United States Railroad Retirement Board v. American Railroads Corporation, U.S.D.C., N.D. ILL., No. 03C 2156 (May 7, 2003).

The evidence supplied by Mr. McClure and counsel in April 2003 as a result of the District Court action is that American Railroads was incorporated as a privately held corporation by Mr. McClure, Mr. Geib, and Mr. Minton on October 15, 1990, and first compensated employees in November 1990. Mr. McClure stated approximately 40 percent of American Railroads revenue derived "from the GC &SS Railway in 2002" and 5 percent from "3rd party switching companies"; but counsel for American Railroads subsequently stated in clarification that American Railroads "provides services and generates its revenues" from Mo&VP RR, GC&SS Railway, and Sweetwater Switching. The services are described as: sales assistance and procurement of new customers; tax accounting, including preparing data for outside public accountants; final billings; maintenance of accounting records; preparation of periodic payrolls for

these companies and payroll record keeping; negotiation and procurement of liability and health insurance and administration of insurance claims under these policies; procuring permits, licenses, and legal services; and negotiation on behalf of the rail carriers with the Burlington Northern Santa Fe, the Union Pacific Railroad, and with customers of the rail carriers. In furnishing these services, American Railroads officials occasionally visit the railroad's offices.

On June 16, 2003, the Board[1] in B.C.D. 03-56 determined on the basis of the foregoing evidence that American Railroads was a covered employer under the Acts by reason of being under common control with a rail carrier employer, and performing services in connection with transportation of property by rail. Pursuant to section 259.3 of the Board's regulations (20 CFR 259.3), American Railroads made a timely request for reconsideration of the June 2003 decision on June 8, 2004.

Section 1(a)(1) of the Railroad Retirement Act (45 U.S.C.§ 231(a)(1)), insofar as relevant here, defines a covered employer as:

> (i) any carrier by railroad subject to the jurisdiction of the Surface Transportation Board under Part A of subtitle IV of title 49, United States Code;
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> (ii) any company which is directly or indirectly owned or controlled by, or under common control with, one or more employers as defined in paragraph (i) of this subdivision, and which operates any equipment or facility or performs any service (except trucking service, casual service, and the casual operation of equipment or facilities) in connection with the transportation of passengers or property by railroad * * *.

Sections 1(a) and 1(b) of the Railroad Unemployment Insurance Act (45 U.S.C §§ 351(a) and (b)) contain substantially similar definitions, as does section 3231 of the Railroad Retirement Tax Act (26 U.S.C. § 3231), which is administered by the Internal Revenue Service of the Department of Treasury.

On reconsideration, American Railroads contends that it meets neither of the two elements necessary for it to be covered as a rail carrier affiliate under section 1(a)(1)(ii) above. The Board disagrees with American Railroad's contentions in both respects.

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[1] B.C.D. 03-56 was rendered by two Board members due to the temporary vacancy of the position of Chairman

I. Common Control.

American Railroads' submission on reconsideration does not dispute that Richard McClure, Robert J. Geib, and Michael Minton are majority shareholders of both GC & SS Railway and American Railroads. Rather, American Railroads points to a provision of Texas law which requires in pertinent part that "All the corporate powers of every railroad corporation shall be vested in and be exercised by the legally constituted board of directors. * * *A majority of said directors shall be resident citizens during their continuance as such directors." Vernon's Ann. Civil Statutes Article 6288. Without stating the total number of directors of American Railroads and of GC & SS Railway, the request for reconsideration contends that Mr. McClure, Mr. Geib and Mr. Minton pursuant to VACS Article 6288 do not constitute the majority of directors of GC & SS Railway, and consequently do not control both companies under Texas law. Without control of both companies as defined by Texas law, it is argued that GC & SS Railway cannot be under common control.

The question is not, however, whether control is exercised under Texas law, but under the Railroad Retirement and Railroad Unemployment Insurance Acts. It is not unusual for Federal statues and regulations to establish standards for determining corporate ownership and control in place of considerations under State corporations law. See, e.g., section 1563 of the Internal Revenue Code (26 U.S.C. § 1563) and regulations promulgated thereunder at 26 CFR 1.1563-1 (defining controlled group and rules for determining stock ownership); and 49 U.S.C. § 10102(3) and 49 CFR Part 1185 (pertaining to Surface Transportation Board regulation of companies with interlocking directorates). Pursuant to its authority under section 7(b)(5) of the Railroad Retirement Act, the Board has also promulgated regulations[2] defining "control":

[2] The Board notes that its regulations defining control and common control have remained virtually unchanged for over 60 years (see 4 Fed. Reg. 1477, April 7, 1939) and thus represent the Board's "longstanding" interpretation of the coverage provisions. Barnhart v. Walton, 535 U.S. 212, (2002) at 219

> 202.4 Control.
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> A company or person is controlled by one or more carriers, whenever there exists in one or more such carriers the right or power by any means, method or circumstance, irrespective of stock ownership to direct, either directly or indirectly, the policies and business of such a company or person and in any case in which a carrier is in fact exercising direction of the policies and business of such a company or person.

The Board's regulations promulgated under section 12(l) of the Railroad Unemployment Insurance Act adopt this definition for purposes of determining employers subject to that Act as well. See 20 CFR 301.4. Moreover, regulations of the Internal Revenue Service promulgated under the Railroad Retirement Tax Act contain a similar definition of control at 26 CFR 3231(a)-1:

> * * * the term "controlled" includes direct or indirect control, whether legally enforceable and however exercisable or exercised. The control may be by means of stock ownership, or by agreements, licenses, or any other devices which insure that the operation of the company is in the interest of one or more carriers. It is the reality of control, however, which is decisive, not its form nor the mode of its exercise.

Court decisions under the Railroad Retirement and Unemployment Insurance Acts have found common control to exist where controlling stock ownership of a car and locomotive repair company and a rail carrier lay in the hands of the same individual, Livingston Rebuild Center v. Railroad Retirement Board, 970 F. 2d 295, (7th Cir., 1992); and where a rail carrier funded a revocable trust to purchase and hold stock of a freight forwarding company, Universal Carloading & Distributing Co. v. Railroad Retirement Board, 172 F. 2d 22 (D.C. Cir., 1948). In this case, American Railroads and GC & SS Railway are closely held corporations with the majority of stock held by the same three individuals. The Board finds this constitutes control within the meaning of section 1(a)(1)(ii) of the Railroad Retirement Act, section 1(a) of the Railroad Unemployment Insurance Act, and the regulations promulgated thereunder. Moreover, though American Railroads never responded to the Board's inquiry of August 16 as to the name and position of any individuals jointly holding positions as officers of American Railroads and any rail carriers, it is at least clear that Mr. McClure is President and CEO of both corporations. Further, in his May 21, 2001 response as President and CEO of the private carrier Southern California Railroad, Mr. McClure stated

American Railroads "owns 100%" of the GC&SS Railway, Sweetwater Switching, and Texas North Orient. Even if inaccurate, this statement indicates that Mr. McClure viewed all four companies as one operation. The Board therefore finds that on these facts, control of American Railroads is in the same persons as that by which GC&SS Railway is controlled. See regulations of the Board at 20 CFR 202.5. For the same reasons, American Railroads is under common control with the Texas and North Orient Corporation, which operated as a rail carrier at least through sometime in 2002 and evidently remains in existence at this time.

American Railroads independently argues that the United States Court of Appeals for the Federal Circuit holding in Union Pacific Corporation v. United States, 5 F.3d 523 (Fed Cir. 1993), as previously applied by the Board, dictates that it is not under common control with its wholly owned subsidiary Mo&VP RR. The Union Pacific Corporation decision concerned a parent company which performed services for its wholly owned subsidiary. The Federal Circuit held that as common control meant "mutual subordinance to a controlling principal"(5 F. 3d at 525), a parent corporation is not under common control with its subsidiary within the meaning of section 3231 of the Railroad Retirement Tax Act. However, it has been held under the Tax Act that where the parent company of the rail carrier is itself controlled by another entity, the holding in Union Pacific Corporation does not apply. Thus, in Carland, Inc. and Southern Group, Inc. v. United States, No. 93-0277-CV-W-2, 1995 U.S. Dist. LEXIS 2350, (W. Dist. Mo., February 14, 1995), parent company Kansas City Southern Industries owned subsidiaries Kansas City Southern Railway and Southern Group, Inc. Southern Group in turn was parent to Carland, Inc. The District Court found that although Southern Group was not parent to KCS Railway, KCS Industries was parent to both, and therefore controlled Carland through its ownership of Southern Group just as it controlled its direct subsidiary KCS Railway. Earlier this year, another District Court reached the same conclusion in a case tried solely on the issue of common control under the Railroad Retirement Tax Act. See: Trans-Serve Inc. v. United States, No. 00-1017, 2004 U.S. Dist. LEXIS 7784, (W.D. La., March, 31, 2004). The facts were essentially the same as in Carland. Kansas City Southern Industries, direct parent corporation of KCS Railway, also owned subsidiary Southern Industrial Services, Inc. Southern Industrial in turn was parent to Trans-Serve, Inc. Here, plaintiff Trans-Serve expressly argued Union Pacific Corporation required the corporate affiliate to be in a parallel corporate position to the rail carrier. Relying on sections 202.4 and 202.5 of the Board's regulations and Universal Carloading, supra, the District Court noted the fact that "if the parent company becomes displeased with a director or officer, as the sole shareholder, the company could remove the individual through a shareholder vote." The District Court concluded "That is the essence of control."

In light of the District Court decision in Trans-Serve, and in co-ordination with the interpretation of the analogous provision of the Railroad Retirement Tax Act by the Internal Revenue Service, approved by the District Courts in Trans-Serve and in the Carland case, the Board concludes that the holding in Union Pacific Corporation does not pertain where the parent company in question is itself subject to control through stock ownership by another corporation. Moreover, because section 202.5 of the Board's regulations defines common control to include wherever control lies "in the same person, persons, or company", the controlling stock ownership may also lie in individual hands rather than in another corporation. See B.C.D. 96-20, *Escanaba Services, Inc.*, and B.C.D. 96-25, *Rail Investments, Inc.*, (holding Union Pacific Corporation did not prevent a finding of common control where the sole shareholder of the non-carrier was also one of three individual shareholders who controlled a rail carrier through a voting trust, and were officers of the rail carrier and the affiliate). In this case, Richard McClure, Robert J. Geib, and Michael Minton as majority shareholders of both GC & SS Railway and American Railroads stand in the same place with respect to Mo&VP RR as Kansas City Southern Industries did as owner of Southern Industries and KCS Railway with respect to Trans-Serve. Accordingly, the Board finds on these facts that American Railroads is under common control with Mo&VP RR as well.[3] For the same reason, American Railroads is also under common control with GC & SS Railway subsidiary rail carrier Sweetwater Switching.

II. Service in connection with railroad transportation.

Aside from whether common control exists, American Railroads argues that it does not perform services in connection with railroad transportation. It contends that the services it performs are not "specific services in connection with the physical operation of the railroad". However, section 202.7 of the Board's regulations defines a service as "in connection with railroad transportation * * * if such service or operation is reasonably directly related, functionally or economically, to the performance of obligations which a company or person * * * have undertaken as a common carrier by railroad * * * ." See 20 CFR 202.7. The Court of Appeals for the Eighth Circuit found operation of an office building which housed administrative offices of the rail carrier to be "a service connected with and supportive of railroad transportation." Southern Development Co. v. Railroad Retirement Board, 243 F. 2d 351, (8th Cir., 1957) at

[3] The coverage decision in B.C.D. 95-23, *Pioneer Railcorp*, cited by American Railroads in the reconsideration request, does not require a different result, since there is no indication in that decision that the parent company was itself controlled by another entity or group.

355. If such an indirect activity as maintaining space for office employees constitutes a service with the meaning of the Acts, the Board is then convinced that the actual activities of those office employees, such as the sales, payroll, insurance, and record keeping functions and other activities listed above which American Railroads conducts for the affiliated rail carriers, must be services in connection with the rail transportation of GC &SS Railway, Mo&VP RR and Sweetwater Switching as well. See B.C.D. 03-76, *Canadian National Railway Properties, Inc.* (affiliate company which acquired, managed and disposed of real estate and personal property performed a service in connection with the railroad transportation conducted by the associated rail carrier.)

In his May 21, 2001 letter noted above, Mr. McClure stated these railroads, plus the Texas North Orient, "all create revenues through American Railroads Corporation". Later, in the first response dated April 2, 2003 to the contumacy action in District Court, Mr. McClure as Chairman, President and CEO of American Railroads, stated that 40 percent of American Railroads revenue derives from the GC&SS Railway, and 5 percent from "3rd party switching companies". In the second response to the contumacy action dated April 28, 2003, counsel for American Railroads clarified that "American Railroads Corporation (ARC) provides services and generates its revenues from these [above named] affiliated and owned companies." Based on the foregoing, the Board therefore finds that American Railroads provides a service in connection with the transportation of property by rail which is not casual in nature. See regulations of the Board at 20 CFR 202.6.

Accordingly, on reconsideration, the Board concludes that American Railroads Corporation is an employer covered by the Railroad Retirement and Railroad Unemployment Insurance Acts, and is required to file returns of service and make such contributions as are required of employers under the Acts. In that respect, the last question remaining is the effective date of coverage. We determined in B.C.D. 03-56 that because GC&SS Railway became a covered employer May 11, 1993, American Railroads first came under common control and began to perform services in connection with the rail transportation conducted by an affiliated rail carrier on that date. On further review, however, the evidence is that American Railroads was formed in 1990, and shareholders McClure, Geib and Minton formed Texas North Orient Corporation in 1991, placing American Railroads under common control with a rail carrier for which it performed services in 1991 rather than in 1993 when GC&SS Railway later began operations. The Board therefore finds on reconsideration that the correct

effective date of coverage under the Acts is June 1, 1991, the date Texas North Orient Corporation began operations as a rail carrier employer. As we noted in our initial decision in B.C.D. 03-56, service and compensation may be credited to American Railroads employees from the earlier date to the extent permitted by section 9 of the Railroad Retirement Act and regulations of the Board at 20 CFR 211.16.

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